

CREDIT OPINION

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Bothell (City of) WA

Update to credit analysis of Bothell (City of), Washington

Summary

The City of Bothell (Aa2) has a large wealthy tax base supported by a robust technology corridor as well as its inclusion in the Puget Sound economy, and a pressured financial position with support from significant funds outside of the city's operating funds that is expected to move to structural balance in the medium term. The rating additionally incorporates the city's manageable debt burden.

On December 19, we assigned a Aa2 issuer rating and affirmed the Aa2 rating on the city's \$35.9 million in outstanding general obligation limited tax (GOLT) bonds.

Credit strengths

- » Large and growing tax base with affluent population
- » Significant available reserves outside of city operating funds

Credit challenges

- » Currently weak financial position compared to many peers, though expected to improve significantly
- » Current service delivery levels straining operating budget

Rating outlook

Outlooks are not normally assigned to issuers with this amount of debt outstanding.

Factors that could lead to an upgrade

- » Material improvement in the city's reserve position
- » Continued robust growth in the city's tax base

Factors that could lead to a downgrade

- » Deterioration of the city's reserve position
- » Material decline in the city's tax base

Key indicators

Exhibit 1

Bothell (City of) WA	2012	2013	2014	2015	2016
Economy/Tax Base					
Total Full Value (\$000)	\$5,907,643	\$5,804,636	\$6,128,996	\$7,651,204	\$8,296,058
Population	-	34,220	34,920	41,207	43,980
Full Value Per Capita	\$175,488	\$169,627	\$175,515	\$185,677	\$188,633
Median Family Income (% of US Median)	136.1%	144.1%	151.6%	154.3%	154.3%
Finances					
Operating Revenue (\$000)	\$36,804	\$40,001	\$43,937	\$45,833	\$47,927
Fund Balance (\$000)	\$7,437	\$2,951	\$2,697	\$5,399	\$4,437
Cash Balance (\$000)	\$3,551	\$3,023	\$5,284	\$5,714	\$5,307
Fund Balance as a % of Revenues	20.2%	7.4%	6.1%	11.8%	9.3%
Cash Balance as a % of Revenues	9.6%	7.6%	12.0%	12.5%	11.1%
Debt/Pensions					
Net Direct Debt (\$000)	\$33,225	\$48,193	\$46,743	\$95,134	\$91,962
3-Year Average of Moody's ANPL (\$000)	\$29,645	\$40,444	\$54,282	\$74,806	\$91,137
Net Direct Debt / Operating Revenues (x)	0.9x	1.2x	1.1x	2.1x	1.9x
Net Direct Debt / Full Value (%)	0.6%	0.8%	0.8%	1.2%	1.1%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.8x	1.0x	1.2x	1.6x	1.9x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.5%	0.7%	0.9%	1.0%	1.1%

Source: City of Bothell and Moody's Investors Service

Profile

The City of Bothell is a wealthy community located in the Puget Sound about 17 miles northwest of Seattle (Aaa stable), 12 miles north of Bellevue (Aaa stable) and 17 miles south of Everett. The city lies in both King (Aaa stable) and Snohomish (Aa2 stable) counties. The city is a full service municipal entity and covers 13.7 square miles and has a population of 43,000.

Detailed credit considerations

Economy and Tax Base: Large and growing Puget Sound tax base with above average resident wealth levels

The city is located in the greater Puget Sound area and has a vibrant and expanding local economy. The city's tax base is large and growing, with 2017 assessed value at \$9.9 billion, an increase of 19.3% over 2016 and 43% higher than its pre-recession peak of \$6.9 billion in 2009. Recent growth has been robust with a 5-year average annual growth of 7.5% which we expect will continue in the near to medium term. The local economy will continue to be driven by the Bothell Technology Corridor, a state-designated innovation partnership zone facilitated by University of Washington-Bothell, Cascadia College and private sector businesses. The city has also invested significant funds in the revitalization of downtown and should see significant economic growth from this investment. Local residents further benefit from the employment opportunities across the Puget Sound area as evidenced by the low 4% unemployment rate as of October 2017. The city is an affluent community with the median family income of residents at an above-average \$101,872 or 154.3% of the US and 2017 full value per capita, a proxy measure of wealth, is a strong \$225,019.

Financial Operations and Reserves: Narrowed financial profile that is expected to improve; Significant available reserves outside the General Fund

The city's financial profile has narrowed recently as the city has had to spend down reserves to maintain current service delivery levels, however going forward the city has worked to stabilize its financial profile through one-time cash infusions and new and potential ongoing revenue sources. The city will also see continued increases in revenues as the Puget Sound economy continues to expand.

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On an operating fund (General Fund, Asset Replacement Fund and Debt Service Fund) basis the city's reserve position is weak, with available reserves at only 9.3% of revenues. However, inclusive of the city's \$8 million in reserves held in the capital improvement fund that are available for operations the city has 25.9%, a level that is in line with rated peers. On an operating basis, the city had a \$897,000 use of reserves in 2016. The city's capital plan and general service delivery contributed to the deficit, however, city management is working to align ongoing expenditures with ongoing revenues. To aid in future service delivery, the city passed a safe streets and sidewalks levy in 2016 that will yield approximately \$4.5 million per year initially and cover street maintenance costs that had traditionally come from the general fund that started in 2017. The city is further pursuing a public safety levy in 2018 that will help alleviate future cost of service. Passage of this levy will greatly enhance the city's expenditure flexibility and allow management to build up reserves and maintain the city's financial profile.

Going forward the city has significant available one-time revenue streams as it maintains an estimated \$7-11 million in property that it plans to sell to developers over the next 5 years. These properties act as a reserve to protect the city against future financial stress if the projected ongoing revenue streams do not come to fruition. The city has budgeted contingencies that adjust service delivery levels based on its success in obtaining ongoing revenue and shows the city balancing its budget under several scenarios. The city's ability to leverage its one-time revenue and potential ongoing revenue to move to balanced operations and maintain fund balances in-line with Aa2-rated peers will drive future reviews.

LIQUIDITY

The city's 2016 operating fund liquidity was narrow at 11.1% of revenues, however inclusive of available funds held in the capital improvements fund the city has \$13.3 million or 27.8% of operating revenues.

Debt and Pensions: Average debt burden, no plans for future debt

The city's debt consists primarily of non-voted, limited tax general obligation bonds totaling \$35.9 million and a lease revenue bond with \$48.6 million remaining for the City Hall facility issued in 2014. This debt plus the city's \$6.7 million in construction loans equals an average debt burden of .9% of 2017 full value and 1.9 times operating revenues. The city's debt burden should decline going forward as the city has no current debt plans and will continue to pay down the existing debt. The city does have some capital needs to address however the city's capital plan outlines non-debt revenue streams to handle these.

DEBT STRUCTURE

The city's LTGO debt has level debt service out to 2022 at which point debt service ramps down through maturity in 2040. The city hall lease has level debt service out through 2032 at when it ramps down through maturity in 2040.

DEBT-RELATED DERIVATIVES

The city does not have any debt-related derivatives.

PENSIONS AND OPEB

The city is a participant in Washington's retirement systems for several defined-benefit pension plans. Most employees are enrolled in Public Employees Retirement System (PERS) plans and public safety employees are enrolled in the system's related specialty plans (LEOFF and PSERS, respectively). Based upon Moody's standard adjustments to reported pension data, the city's three-year average adjusted net pension liability (ANPL) was manageable at 1.9x operating funds revenues and 1.1% of full value. Additionally, the city also provides other post-employment benefits (OPEB) of health care for public safety retirees, as required by state statutes. The obligation is funded on a pay-go basis and the city contributed \$163,000 in 2016.

Management and Governance

Washington cities have an institutional framework score of 'Aa', or strong. Despite some sales tax volatility, cities benefit from property tax levies whereby collections can be increased up to 1% of the prior year. Cities have both the ability and willingness to make mid-year budgetary reductions.

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